



DEPARTMENT OF THE TREASURY

Internal Revenue Service

26 CFR Part 1

Apportionment of Tax Items Among the Members of a Controlled Group of
Corporations

CFR Correction

In Title 26 of the Code of Federal Regulations, Part 1 (§1.1551 to End of Part 1), revised as of April 1, 2011, on page 24, in §1.1561-2, paragraphs (c) through (f) are added to read as follows:

§1.1561-2 Special rules for allocating reductions of certain section 1561(a) tax-benefit items.

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(c) *Accumulated earnings credit.* The component members of a controlled group of corporations are permitted to allocate the amount of the accumulated earnings credit unequally if they have an apportionment plan in effect.

(d) [Reserved]

(e) *Short taxable years not including a December 31st date—*(1) *General rule.* If a corporation has a short taxable year not including a December 31st date and, after applying the rules of section 1561(b) and paragraph (e)(2)(i) of this section, it qualifies as a component member of the group with respect to its short taxable year (short-year member), then, for purposes of subtitle A of the Internal Revenue Code, the amount of any tax-benefit item described in section 1561(b) allocated to that component member's short taxable year shall be the amount specified in section 1561(a) for that item, divided by the number of corporations which are component members of that group on the last day of that component member's short taxable year. The component members of such group may not apportion, by an apportionment plan, an amount of such tax-benefit item to any short-year member that differs from equal apportionment of that item.

(2) *Additional rules.* For purposes of paragraph (e)(1) of this section—

(i) Section 1563(b) shall be applied as if the last day of the taxable year of a short-year member were substituted for December 31st; and

(ii) The term short taxable year does not refer to any portion of a tax year of a corporation for which its income is required to be included in a consolidated return pursuant to § 1.1502-76(b).

(3) *Calculation of the additional tax.* A short-year member (as defined in paragraph (e)(1) of this section) for its short taxable year calculates its additional tax liability imposed by section 11(b)(1) only on its own income, and therefore the subsequent calculation of the additional tax liability with regard to the remaining members of the group will not include the income of this short-year member.

(4) *Calculation of the alternative minimum tax.* If a component member has a tax year of less than 12 months, whether or not such tax year includes a December 31st date, see section 443(d) for the annualization method required for calculating the alternative minimum tax.

(5) *Examples.* The provisions of this paragraph (e) may be illustrated by the following examples:

Example 1. Formation of a new member of a controlled group—(i) *Facts.* On January 2, 2007, corporation X transfers cash to newly formed corporation Y (which begins business on that date) and receives all of the stock of Y in return. X also owns all of the stock of corporation Z on each day of 2006 and 2007. X, Y and Z have an apportionment plan in effect, apportioning the 15 percent

taxbracket amount as follows: 40% (\$20,000) to each of X and Y and 20% (\$10,000) to Z. X, Y and Z each file a separate return with respect to the group's December 31st, 2007 testing date. X is on a calendar tax year and Z is on a fiscal tax year ending on March 31. Y adopts a fiscal year ending on June 30 and timely files a tax return for its short taxable year beginning on January 2, 2007, and ending on June 30, 2007.

(ii) *Y's short taxable year.* On June 30, 2007, Y is a component member of a parent subsidiary controlled group of corporations composed of X, Y and Z. Pursuant to paragraph (e)(1) of this section, the group may not apportion any amount of the 15 percent tax bracket to Y's short taxable year ending on June 30, 2007. Rather, Y is entitled to exactly 1/3 of such bracket amount, or \$16,667.

(iii) *The members' subsequent tax years.* On December 31st, 2007, X, Y and Z are component members of a parent-subsidiary controlled group of corporations. For their tax years that include December 31st, 2007 (X's calendar year ending December 31st, 2007, Z's fiscal year ending March 31, 2008 and Y's fiscal year ending June 30, 2008), X, Y and Z apportion among themselves the full amount of all of the applicable tax brackets pursuant to their apportionment plan. For example, 40% of the 15 percent tax-bracket amount, or \$20,000, was apportioned to each of X and Y, and the remaining 10%, or \$10,000, was apportioned to Z.

Example 2. Allocating a tax bracket to the short taxable year of a liquidated member of a controlled group--(i) *Facts.* On January 1, 2007, corporation P owns all of the stock of corporations S₁, S₂ and S₃ (the P group). Each of these four component members of the P group, with respect to the group's December 31st, 2007 testing date, files its separate return on a calendar year basis. These members have an apportionment plan in effect (the P group plan) under which S₁ and S₂ are each entitled to 40% of the 15 percent tax-bracket amount (\$20,000), and P and S₃ are each entitled to 10% of the 15 percent tax-bracket amount (\$5,000). On May 31, 2007, S₁ liquidates and therefore files a return for the short taxable year beginning on January 1, 2007, and ending on May 31, 2007. On July 31, 2007, S₂ liquidates and therefore files a return for the short taxable year beginning on January 1, 2007 and ending on July 31, 2007. P and S₃ each file a return for their 2007 calendar tax years.

(ii) *Apportionment of the 15 percent tax bracket to S₁ for its short taxable year.* On May 31, 2007, S₁ is a component member of the P group composed of P, S₁, S₂ and S₃. Pursuant to paragraph (e)(1) of this section, the group may not apportion any amount of the 15 percent tax bracket to S₁'s short taxable year ending on June 30, 2007. Rather, S₁ is entitled to exactly 1/4 of such bracket amount, or \$12,500.

(iii) *Apportionment of the 15 percent tax bracket to S₂ for its short taxable year.* On July 31, 2007, S₂ is a component member of the P group composed of P, S₂ and S₃. Pursuant to paragraph (e)(1) of this section, the group may not apportion any amount of the 15 percent tax bracket to S₂'s short taxable year ending on June 30, 2007. Rather, S₂ is entitled to exactly 1/3 of such bracket amount, or \$16,667.

(iv) *Apportionment of the 15 percent tax bracket to P and S₃ for each of their calendar tax years.* On December 31st, 2007, P and S₃ are component members of the P group. Accordingly, for P and S₃'s 2007 calendar tax year, they are each apportioned \$25,000 of the 15 percent tax bracket, pursuant to the applicable P group plan.

Example 3. Liquidation of member after its transfer to another controlled group--(i) *Facts.* The facts are the same as in Example 2, except that P, on April 30, 2007, sold all of the stock of S₂ to the M-N controlled group. At the time of the sale, M and N are both unrelated to any members of the P group. As in Example 2, S₂ liquidates on July 31, 2007, and therefore files a tax return for its short taxable year beginning on January 1, 2007, and ending on July 31, 2007. Pursuant to the sales agreement, the M-N group timely notified P that S₂ had liquidated.

(ii) *Controlled group analysis.* On April 30, 2007, the date of the sale of S₂, the P group reasonably expected that S₂ would be treated as an excluded member with respect to its December 31st, 2007 testing date. On that April 30th date, S₂ had been a member of the P group for less than one-half the number of days of what it expected would be a full 2007 calendar tax year preceding December 31st, 2007 (120 days (January 1-April 30) out of 364 days (January 1-December 30)). Yet, as a result of S₂'s subsequent liquidation by the M-N group prior to December 31st, 2007, S₂ became a component member of the P group with respect to the P group's December 31st, 2007 testing date. With respect to that December 31st testing date, S₂ thus was a member of the P group for more than one-half of the number of days of its tax year ending on July 31, 2007, which days preceded December 31st, 2007 (120 days (January 1-April 30 of 2007) out of 211 days (January 1-July 30 of 2007)). The allocation of the 15 percent tax-bracket amount to the P group members is determined in the same manner as in Example 2 and, therefore, the bracket amounts allocated to P, S₁, S₂ and S₃ are the same as determined in Example 2. The allocation of the bracket amounts would be the same if, at the time P sold all of the S₂ stock, the parties had made a section 338(h)(10) election.

Example 4. Short tax year including a December 31st date. Corporation X owns all of the stock of corporations Y and Z. X, Y and Z each file separate returns. X and Y are on a calendar tax year and Z is on a fiscal tax year beginning October 1 and ending September 30. On January 2, 2007, Z liquidates. Because Z's final tax year (beginning on October 1, 2006 and ending on January 2, 2007) includes a December 31st date, that is, December 31, 2006, it is therefore not subject to the short taxable year rule provided by section 1561(b) and paragraph (e) of this section. Accordingly, Z is a component member of the X-Y-Z group, for the group's December 31st, 2006 testing date. Thus, the rules of this paragraph (e) do not limit the amount of any of the tax-benefit items of section 1561(a) available to Z or to this controlled group.

(f) *Effective/applicability date.* This section applies to any tax year beginning on or after December 21, 2009. However, taxpayers may apply this section to any Federal income tax return filed on or after December 21, 2009. For tax years beginning before December 21, 2009, see § 1.1561-2T as contained in 26 CFR part 1 in effect on April 1, 2009.

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